

## Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 CIEP-01 SP-02 STR-04 TRSE-00

LAB-04 SIL-01 SAM-01 OMB-01 AGR-05 USIA-06 NSC-05

SS-15 /081 W

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R 151752Z APR 76

FM USMISSION EC BRUSSELS

TO SECSTATE WASHDC 1008

INFO ALL EC CAPITALS 2022

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E.O. 11652: NA

TAGS: EFIN EEC

SUBJECT: EC COMMISSION'S MEDIUM-TERM ECONOMIC PROJECTIONS

REF: EC BRUSSELS 1384

1. BEGIN SUMMARY: AN INTERNAL COMMISSION ASSESSMENT OF EC ECONOMIC PROSPECTS FORESEES AN OVERALL 4.4 PERCENT REAL GROWTH RATE PER YEAR FOR THE EC FROM 1976-1980. UNEMPLOYMENT AND PRICE INFLATION WILL CONTINUE TO BE SERIOUS PROBLEMS. IN FACT, CURRENT DISPARITIES BETWEEN MEMBER STATE ECONOMIES ARE LIKELY TO WIDEN WHICH WILL IMPEDE EC COHESION. THE EC IS CURRENTLY DRAWING UP A POLICY PROGRAM TO COUNTERACT THESE PROBLEMS. END SUMMARY.

2. SLOWER GROWTH RATE: COMMISSION FINANCIAL OFFICIALS HAVE JUST COMPLETED AN ASSESSMENT OF EC ECONOMIC PROSPECTS FOR 1976-1980. THE FIVE-YEAR GROWTH RATE IS SLIGHTLY BELOW THE PREVIOUS LONG-TERM TREND. THE EC CONSEQUENTLY WOULD NOT RECOVER THE LOSSES SUFFERED FROM THE RECESSION. THIS IS ATTRIBUTABLE TO A SLOWDOWN IN EC POTENTIAL GROWTH AND FAILURE TO USE FULLY EXISTING EXCESS CAPACITY. COMMISSION PROJECTIONS SHOW AN ANNUAL AVERAGE EC REAL GROWTH RATE OF 4.4 PERCENT FOR THE PERIOD. THE UK, IRELAND AND LUXEMBOURG WOULD HAVE

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ANNUAL RATES OF 3.5 PERCENT; FRANCE, 5.5 PERCENT; AND THE

OTHER MEMBER STATES, 4-5 PERCENT. THESE PROJECTIONS ASSUME AN AVERAGE GROWTH IN THE VOLUME OF WORLD TRADE OF 8-8.5 PERCENT AND AN AVERAGE GDP PRICE DELATOR FOR MAJOR INDUSTRIAL COUNTRIES OF 7-8 PERCENT PER YEAR FOR THE PERIOD.

3. HIGH UNEMPLOYMENT: THE STUDY FORECASTS THE PERSISTENCE OF HIGH UNEMPLOYMENT LEVELS, BECAUSE OF THE FOLLOWING FACTORS: (1) INVESTMENT ACTIVITY WILL BE SLOE TO RECOVER; (2) LABOR COSTS ARE HIGH; (3) LABOR SUPPLY WILL INCREASE; AND (4) A LARGE NUMBER OF WORKERS ARE CURRENTLY ON SHORT TIME. THUS, THE EC UNEMPLOYMENT RATE WILL BE ABOUT 3.2 PERCENT IN 1980, COMPARED TO 4 PERCENT IN 1975 AND RATES OF 1.5-2 PERCENT IN THE 1960'S. THE NETHERLANDS AND IRELAND ARE NOT LIKELY TO REDUCE THEIR CURRENT UNEMPLOYMENT LEVELS; ITALY'S RATE WILL RISE. THE STUDY CONCLUDES THAT THE MAJRO ECONOMIC POLICY PROBLEM FACING THE EC WILL BE ACHIEVING A RETURN TO FULL EMPLOYMENT.

4. PRICE INFLATION AND BOP: THE EC AVERAGE RATE OF PRICE INFLATION, BASED ON THE GDP DEFLATOR, SHOULD BE 7.5 PERCENT PET YEAR, BUT MEMBER STATE RATES WILL VARY SHARPLY. THE FRG WILL BE THE ONLY MEMBER STATE SIGNIFICANTLY BELOW THE PROJECTED EC AVERAGE WHILE ITALY, AND THE UK, AND IRLEAND WILL HAVE HIGHER RATES. ALMOST ALL STATES, HOWEVER, ARE ESTIMATED TO ACHIEVE EQUILIBRIUM OR A SURPLUS IN THEIR BALACNE OF PAYMENTS (BOP) ON CURRENT ACCOUNT BY 1980. THIS FORECAST IS BASED ON THE FOLLOWING ASSUMPTIONS: (1) OPEC WILL BE IN EQUILIBRIUJ ON CURRNT ACCOUNT IN 1980 WITH THE INDUSTRIALIZED COUNTRIES; (2) DEVELOPMENT AID WILL REMAIN AT ABOUT CURRENT LEVELS; (3) THE EC WILL HAVE A TRADE SURPLUS WITH EASTERN EUROPE; AND (4) EC TRADE WITH INDUSTRIALIZED COUNTRIES WILL SUSTAIN A GROWTH RATE OF ABOUT 7-8 PERCENT PER YEAR.

5. EC DIFFICULTIES: THE STUDY CONCLUDES THAT THE GAP BETWEEN MEMBER STATE INCOME LEVELS WILL WIDEN. IN ADDITION, MEMBER STATE COST AND PRICE TRENDS WILL CONTINUE TO DIVERGEM THESE TRENDS WILL IMPEDE ECONOMIC POLICY COORDINATIONA DN EC INTEGRATION EFFORTS. THUS, WITHOUT A CHANGE IN ECONOMIC POLICIES, EC COHESION WILL BE IN JEOPARDY.

6. POLICY PROGRAM: THE EC IS CURRENTLY DRAWING UP A FOURTH LIMITED OFFICIAL USE

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MEDIUM-TERM ECONOMIC POLICY PROGRAM, 1976-1980, TO ATTACK ITS ECONOMIC PROBLEMS. THE MISSION HAS OBTAINED A COPY OF THE FIRST CONFIDENTIAL COMMISSION DRAFT OF THIS PROGRAM. (COPIES HAVE BEEN SENT TO INTERESTED AGENCIES, INCLUDING STATE/REP-CLARK AND CEA-JUNZ.) THE COMMISSION AND MEMBER STATES WILL NOW REVIEW THIS DRAFT BEFORE THE COUNCIL IS ASKED TO FORMALLY ADOPT THE PROGRAM. THE SUGGESTED POLICIES ARE CONSEQUENLTLY LIKELY TO BE REVISED. THE CURRENT DRAFT EMPHASIZES THE NEED TO GIVE IN-

CENTIVES TO INVESTMENT AND TO CONTROL PRICE INFLATION IF FULL  
EMPLOYMENT AND SUSTAINED GROWTH ARE TO BE ACHIEVED. IT ALSO  
SUGGESTS A FLEXIBLE EXCHANGE RATE POLICY VIS-A-VIS THE DOLLAR WHICH  
WOULD AVOID ERRATIC RATE MOVEMENT. THE DRAFT PROPOSES  
IMPROVING CONTROL OF THE EXPANSION OF INTERNATIONAL  
LIQUIDITY.  
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## Message Attributes

**Automatic Decaptioning:** X  
**Capture Date:** 01 JAN 1994  
**Channel Indicators:** n/a  
**Current Classification:** UNCLASSIFIED  
**Concepts:** ECONOMIC GROWTH, ECONOMIC ESTIMATES, PROGRESS REPORTS, REGIONAL ORGANIZATIONS  
**Control Number:** n/a  
**Copy:** SINGLE  
**Draft Date:** 15 APR 1976  
**Decaption Date:** 01 JAN 1960  
**Decaption Note:**  
**Disposition Action:** RELEASED  
**Disposition Approved on Date:**  
**Disposition Authority:** GolinoFR  
**Disposition Case Number:** n/a  
**Disposition Comment:** 25 YEAR REVIEW  
**Disposition Date:** 28 MAY 2004  
**Disposition Event:**  
**Disposition History:** n/a  
**Disposition Reason:**  
**Disposition Remarks:**  
**Document Number:** 1976ECBRU03881  
**Document Source:** CORE  
**Document Unique ID:** 00  
**Drafter:** n/a  
**Enclosure:** n/a  
**Executive Order:** N/A  
**Errors:** N/A  
**Film Number:** D760144-0803  
**From:** EC BRUSSELS  
**Handling Restrictions:** n/a  
**Image Path:**  
**ISecure:** 1  
**Legacy Key:** link1976/newtext/t19760459/aaaabxqo.tel  
**Line Count:** 122  
**Locator:** TEXT ON-LINE, ON MICROFILM  
**Office:** ACTION EUR  
**Original Classification:** LIMITED OFFICIAL USE  
**Original Handling Restrictions:** n/a  
**Original Previous Classification:** n/a  
**Original Previous Handling Restrictions:** n/a  
**Page Count:** 3  
**Previous Channel Indicators:** n/a  
**Previous Classification:** LIMITED OFFICIAL USE  
**Previous Handling Restrictions:** n/a  
**Reference:** 76 EC BRUSSELS 1384  
**Review Action:** RELEASED, APPROVED  
**Review Authority:** GolinoFR  
**Review Comment:** n/a  
**Review Content Flags:**  
**Review Date:** 30 MAR 2004  
**Review Event:**  
**Review Exemptions:** n/a  
**Review History:** RELEASED <30 MAR 2004 by ShawDG>; APPROVED <31 MAR 2004 by GolinoFR>  
**Review Markings:**

Margaret P. Grafeld  
Declassified/Released  
US Department of State  
EO Systematic Review  
04 MAY 2006

**Review Media Identifier:**  
**Review Referrals:** n/a  
**Review Release Date:** n/a  
**Review Release Event:** n/a  
**Review Transfer Date:**  
**Review Withdrawn Fields:** n/a  
**Secure:** OPEN  
**Status:** NATIVE  
**Subject:** EC COMMISSION'S MEDIUM-TERM ECONOMIC PROJECTIONS  
**TAGS:** EFIN, EEC  
**To:** STATE  
**Type:** TE  
**Markings:** Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006